

#49

6/1/65

Memorandum 65-30

Subject: Study No. 49 - Rights of Unlicensed Contractor

Attached is a copy of the research study prepared by our consultant on this topic.

The staff recommends that this topic be dropped from our agenda. We do not believe that the topic is one that is suitable for a Commission recommendation. As noted in the research study at page 9, "the California courts have avoided forfeiture in a large number of cases." See pages 9-12.

In this connection, it should be noted that Section 10136 of the Business and Professions Code provides:

10136. No person engaged in the business or acting in the capacity of a real estate broker or a real estate salesman within this state shall bring or maintain any action in the courts of this state for the collection of compensation for the performance of any of the acts mentioned in this article without alleging and proving that he was a duly licensed real estate broker or real estate salesman at the time the alleged cause of action arose.

If the Commission believes that this topic is a suitable one for a Commission recommendation, the possible solutions identified by the research consultant are set out on pages 18-21 of the Research Study.

Respectfully submitted,

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Executive Secretary

March 6, 1958  
(Revision of 1/28/59)

A STUDY TO DETERMINE WHETHER SECTION 7031  
OF THE BUSINESS AND PROFESSIONS CODE, WHICH  
PRECLUDES AN UNLICENSED CONTRACTOR FROM  
BRINGING AN ACTION TO RECOVER FOR WORK DONE,  
SHOULD BE REVISED.

A study made at the direction of the  
California Law Revision Commission by  
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Study #49

## IN GENERAL

Most states have long required such professional people as dentists, lawyers, doctors, etc., to be licensed. Moreover, licensing schemes covering people engaged in various occupations such as plumbers, electricians, etc., have been in effect since 1885.<sup>1</sup> However, the licensing of contractors did not begin until a relatively recent date. The first statute was passed in North Carolina in 1925.<sup>2</sup> Today contractors are required to be licensed in 19 states,<sup>3</sup> including California.<sup>4</sup> Statutes licensing contractors are justified on the ground that they are necessary to protect the public and building industry from incompetent, inexperienced, unlawful and fraudulent acts of building contractors.<sup>5</sup> It has also been asserted that these statutes protect the building industry from the evils of "cut-throat" competition.<sup>6</sup>

License legislation covering contractors was first enacted in California in 1929.<sup>7</sup> This statute has been amended on several occasions since that time. While California was not the initial state to impose restrictions on contractors, the California legislation was among the first, and it has been used as a model by other states. The constitutionality of the California requirements has been sustained.<sup>8</sup>

### THE CALIFORNIA LICENSING LAW

In order to understand the problems raised by the topic under study it is necessary, or at least desirable, to mention some of the general aspects of the California contractors licensing statutes. An appreciation of the scheme will also make for a clearer understanding of such recommendations as are subsequently made.

The California statutes, unlike those found in some states, cover all

kinds of contractors. Section 7026 of the Business and Professions Code defines a contractor in this way:

The term contractor for the purposes of this chapter is synonymous with the term "builder" and, within the meaning of this chapter, a contractor is any person, who undertakes to or offers to undertake to or purports to have the capacity to undertake to or submit a bid to, or does himself or by or through others, construct, alter, repair, add to, subtract from, improve, move, wreck or demolish any building, highway, road, railroad, excavation or other structure, project, development or improvement, or to do any part thereof, including the erection of scaffolding or other structures or works in connection therewith. The term contractor includes subcontractor and specialty contractor.

Not only must each person who engages in the capacity of a contractor have a license, but two licensed individuals must have an additional license<sup>9</sup> for engaging in a joint venture, partnership, etc.

The administration of the California statutes is exercised by a Contractor's State License Board composed of seven licensed people who are actively engaged in the contracting business, and who have been in business<sup>10</sup> for five years preceding their appointment.

An applicant is required to submit a written application to the board<sup>11</sup> accompanied by an application fee of \$15.<sup>12</sup> The application must include a description of the applicant's contracting business, a designation of the category in which a license is desired, and relevant company names,<sup>13</sup> addresses, etc.

Each applicant is required to possess "good character"<sup>14</sup> and must show "such degree of experience, and such general knowledge of the building, safety, health and lien laws of the State and of the rudimentary administrative principles of the contracting business as the board deems necessary for the safety and protection of the public."<sup>15</sup>

The board is authorized to conduct an investigation of the applicant,<sup>16</sup> and he is required to take an examination.

The license must be renewed each year. Failure to renew within a  
prescribed period is cause for suspension of the license. <sup>17</sup>

The Contractor's State License Board is given the power, along with  
many others, to revoke or suspend a license for various acts such as breach  
of contract, lack of diligence, etc. <sup>18</sup> If a license is revoked or suspended  
the board may require the posting of a bond not exceeding \$1,000 when  
application is thereafter made for a new license. <sup>19</sup>

The board may conduct investigations against licensees upon its own  
motion and must do so when there is a verified complaint filed. <sup>20</sup> Broad  
disciplinary powers are at the disposal of the board. <sup>21</sup>

#### CONSTITUTIONAL LIMITATIONS ON LICENSING

Although the right to enter a profession or occupation is one guaranteed  
by the due process clause of the Fourteenth Amendment, this right is not un-  
qualified. It is subject to such reasonable conditions or restrictions as  
might be imposed by the states under their police powers. Consequently, the  
right of engaging in an occupation or profession must be balanced against the  
duty of the state to protect the health, safety, morals and general welfare  
of the people.

The purpose of licensing depends upon the nature of the public  
interest involved. Thus, plumbing contractors are required to be licensed  
in order to protect the health of the people; whereas, the purpose of the  
contractor-licensing statutes is to protect against pecuniary loss resulting  
from fraud, breach of contract or poor workmanship. But unless some public  
interest is served, a licensing requirement is violative of the guarantees  
of the due process clause. <sup>22</sup> Elsewhere it has been held that statutes requiring  
painters, <sup>23</sup> masons, <sup>24</sup> heating contractors <sup>25</sup> and paper hangers <sup>26</sup> to be licensed are

not constitutional. In California, however, people engaged in these trades along with interior decorators, landscape gardeners, well-drillers, etc. must get licenses. The possibility of abuses among certain tradesmen in California has obviously been made the ground for regulating most of the trades or occupations. Is such extensive legislation consistent with the Constitution? Or, on the other hand, is the Legislature's decision on the desirability of such statutes to be deemed conclusive?

Apparently the Supreme Court of the United States has never ruled on the validity of contractor licensing statutes. However, there have been cases upholding the validity of analogous requirements.<sup>27</sup> As previously noted, it has been held in California that the California statutes are valid.<sup>28</sup> It is questionable whether the older cases, mentioned above, holding certain statutes to be invalid would be followed today. As long as there is an assumption of the likelihood of fraud, breach of contract or poor workmanship on the part of contractors, there is little doubt about their being sustained.

#### ADOPTION OF SECTION 7031

The California Code provides that "any person who acts in the capacity of a contractor without a license, and any person who conspires with another person to violate any of the provisions of this chapter, is guilty of a misdemeanor."<sup>29</sup>

In 1931 a further statute imposing sanctions on the unlicensed contractor was adopted. Minor amendments to this statute have been made several times. Until the last session of the Legislature, Section 7031 read as follows:

No person engaged in the business or acting in the capacity of a contractor, may bring or maintain any action in any court of this

State for the collection of compensation for the performance of any act or contract for which a license is required by this chapter without alleging and proving that he was a duly licensed contractor at all times during the performance of such act or contract.

Generally speaking, the effect of Section 7031 is to deny recovery to an unlicensed contractor.

Section 7068 of the Business and Professions Code requires a licensee to notify the board within 10 days of the departure from employment of his managing employee. In the event this notice is not given the contractor's license is ipso facto suspended. In a recent case a licensee contracted to perform certain work. During the performance of the contract the managing employee left the employ of the licensee. Notice of this fact was not given, nor was a replacement made within a year as required by statute. After the completion of the work suit was brought on a note given as the final payment on the contract. The court held that since the contractor was not duly licensed at all times during the performance of the contract, there could be no recovery.<sup>30</sup> The forfeiture imposed on the contractor in this case resulted in an amendment to Section 7031 by the 1957 Legislature. The amendment consisted of addition of the following:

Until the expiration of six months from the date of a suspension of a license pursuant to Section 7068, the provisions of this section do not apply to any person whose license was suspended pursuant to Section 7068 for failure to notify the registrar within the 10-day period, if such failure was due to inadvertence.<sup>31</sup>

All states having contractor-licensing statutes impose criminal sanctions<sup>32</sup> on the unlicensed contractor. Moreover, most courts refuse to allow the unlicensed contractor to recover on the illegal contract, or in quasi-<sup>33</sup> contract.<sup>34</sup> However, there are only two states, other than California, that have specific statutes denying recovery to an unlicensed contractor.

There is no record showing the origin of the legislation.

### SPECIFIC ISSUE INVOLVED IN STUDY

The purpose of this study is to determine whether Section 7031 of the Business and Professions Code should be further revised or repealed. The problem involved in this study varies greatly from the type of investigations generally made to determine the desirability and effectiveness of a statute. For the most part, the issue raised by Section 7031 is whether there is unjust enrichment when recovery is denied. Specifically the issues are whether it is fair to impose a complete forfeiture on one violating the license law and whether such a harsh sanction is necessary for the enforcement of the applicable license statutes.

### PURPOSE OF SECTION 7031

The primary purpose of the statute under study is to assure the protection and safety of the public.<sup>35</sup> Specifically, it was adopted to protect the public from incompetent or untrustworthy contractors. The Contractor's State License Board is of the opinion that Section 7031 "is actually the teeth in the contractor's license law in that it acts as a deterrent to violations of a criminal nature and therefore places this agency in a better position to regulate the industry pursuant to the statutes."<sup>36</sup>

### RECOVERY ON ILLEGAL CONTRACTS

Section 7031 is, for the most part, expressive of the law followed in the United States even in the absence of a specific statute. Under this prevailing rule the unlicensed contractor, along with other unlicensed persons, is denied recovery on the contract, as well as in quasi-contract.<sup>37</sup> Therefore, generally speaking, Section 7031 does not drastically change the law that would be followed in the absence of it.

The California courts have indicated in numerous cases that an agreement entered into by an unlicensed contractor is illegal. However, there is doubt in this state about the degree of illegality. At times the courts speak of the contract being illegal and void while at other times it is said to be merely malum prohibitum. But irrespective of whether the agreement is malum in se or malum prohibitum Section 7031 provides that there is to be no recovery by an unlicensed contractor. Consequently, the problem of recovery by an unlicensed person in California does not pose the difficulties encountered in other states. For example, it is not necessary to determine whether the California license laws are regulatory or revenue-raising. Nor is there any question about recovery for an occasional or isolated act in this state. Likewise the statute eliminates the difficulty of determining recovery where the contractor was licensed for part of the time that he was performing.

Another difference between the law applied in other states and the provisions of Section 7031 is that elsewhere the courts weight the equities and often allow quasi-contractual recovery in order to avoid forfeiture. This is not always possible under the California statute.

#### APPLICATION OF SECTION 7031

Section 7031 provides that no person may bring an action to collect for the performance of an act for which a license is required unless he alleges and proves that he was a duly licensed contractor at all times during the performance of the contract. Under this provision relief has been denied in suits brought on the contract by an unlicensed contractor. Likewise, it has been held that suit could not be maintained by an assignee of a note given an unlicensed contractor in payment. Nor can there be recovery by an

unlicensed contractor in quasi-contract. The statute also has the effect  
of preventing the foreclosure of a mechanic's lien. Moreover, it is settled  
that Section 7031 is a bar to the enforcement of an arbitration award sought  
by an unlicensed person.

The denial of compensation under Section 7031 has led to some seemingly  
inequitable situations. Among the more drastic ones are the following:

(1) Even though an unlicensed contractor completely performs his side  
of a contract and has received no payment, he is denied recovery.

(2) A partnership has been denied the entire contract price for its  
full performance because of the failure to obtain a partnership license, even  
though one of the partners was apparently a qualified contractor.

(3) A contractor whose license was suspended during performance for  
failure to notify the board within the proper time of the disassociation of  
the managing employee, as required by Section 7068 of the Business and  
Professions Code, was denied recovery even though his license was thereafter  
renewed. The unfair circumstances arising out of the last case prompted the  
1957 amendment to the statute under study. As noted previously, the amendment  
extends the time for giving notice where the managing employee ceases employment.

There are other situations that are apt to arise in which relief could  
not be had because of the requirements of Section 7031. The resulting for-  
feitures would appear to be a high penalty to impose upon the contractor.  
The following are examples:

(1) Suppose that a contractor mistakenly believes that he has complied  
with the licensing requirements. Assume that upon learning of his mistake  
just after he started work under a contract, he complies with the statutory  
provisions. Under Section 7031 there could be no recovery for the work  
performed before the license was obtained nor for that done afterwards.

(2) A contractor whose license is suspended or expires after he has substantially performed his contractual obligations would go without relief because of Section 7031.

(3) The right to sue is also abrogated where two licensed individuals do work as a contractor without taking out a partnership license.<sup>52a</sup>

(4) Suppose a licensed contractor agrees to construct a building. When the building is nearly complete his license is revoked, suspended or expires. There could be no recovery for the work done before or after this time. Assume that the contractor consults with the other party and by mutual agreement the work is continued. Under Section 7031 the contractor could not maintain an action.<sup>53</sup>

(5) If an innocent owner contracts with an unlicensed contractor for the construction of a structure, the owner could apparently sue the contractor for improper performance even though the contractor could not maintain an action for compensation.<sup>54</sup> However in such a case the contractor could set off the value of his services.<sup>54a</sup>

#### JUDICIAL AMELIORATION OF SECTION 7031

Total or partial forfeiture results from precluding an unlicensed contractor from bringing an action. It is well-known that courts abhor forfeitures and they are astute to discover grounds for avoiding them whenever possible. The language of Section 7031 leaves the impression that there is little room for exceptions. However, the California courts have avoided forfeiture in a large number of cases. In fact, there are more reported cases in which the statute has been circumvented than there are denying recovery. The courts have employed a number of devices to avoid forfeiture by the contractor and the corresponding windfall that would go to the other party.

The most frequently used technique for preventing forfeiture under Section 7031 is to find that the person was an employee, or supervisor, and not a contractor. <sup>55</sup> The distinction between these two categories is not at all clear-cut. In fact, there appears to be no apparent difference, practically speaking. As would be expected, a large number of factors have been discussed by the courts in deciding the issue such as: method of compensation, responsibility to subcontractors and material men, right of supervision and whether the party was in the independent business of contracting. However, there is one fact that appears to influence the courts in these cases more than any other. This significant issue is whether the party held himself out as being a licensed contractor. If he did not, he is allowed to recover. This is a most tenuous basis upon which to determine whether there should be a forfeiture under Section 7031. But the result is not entirely irreconcilable if one pauses to consider the penalty that would be inflicted by finding the party to be a contractor. At the same time the parties in these cases appear to be contractors under Section 7026.

In other cases the courts have found that there was merely a sale or an agreement to provide materials and services rather than agreement to perform a job on a contract basis. <sup>56</sup> Sales are not covered by the license laws. <sup>57</sup> I am unable to find any basis upon which to justify the results in this group of cases. There is no difference between an agreement to perform a job for a contract price and one to furnish labor and goods for a specified sum. The cases impress me as being in disregard of the contractor-licensing statutes.

Although the facts indicate a clear violation of the license statutes, there are several cases in which it has been found that there could be <sup>58</sup> recovery because there was substantial compliance with the statutes. In

Citizens State Bank v. Gentry, the contractor's license expired while the work was in progress, but was renewed in the name of a corporation privately owned by the contractor and bearing his name. It was held that the action was not barred in that there had been substantial compliance with the licensing statutes. The same result was reached in Gatti v. Highland Park

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Builders, where licensed contractors conducted a partnership and failed to secure a partnership license. A contractor was also permitted to recover on the basis of substantial compliance in Oddo v. Hedde even though he was not properly licensed to do contracting work. In each of the cases mentioned

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it was emphasized that it would be inequitable to deny recovery. Perhaps this might be so. However, in each of the cases the decision was contrary to the clear and positive language of the statutes. There can be no

substantial compliance with a clearly worded statute. The requirements are either met, or else are not complied with. The reasoning employed in these

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cases would appear to be equally applicable in every instance where a person acting in good faith, or innocently, has failed to comply with the existing statutes. These cases indicate that the courts are reluctant to impose the harsh penalty imposed under Section 7031. Apart from this, there is no basis upon which the cases can be reconciled.

In several cases it has been held that the statute does not bar a suit by an unlicensed subcontractor against an unlicensed general contractor. The reason assigned for this is that the statute was designed for the protection and safety of the public and that purpose is not involved in such an action. Similar reasoning was used to permit one partner of an unlicensed partnership firm to sue the other for an accounting. Lastly, there are two cases in which the unlicensed contractor was the defendant rather than the plaintiff. It was held in both cases that Section 7031 did not apply in such a situation. The plaintiff was not permitted to recover back money paid to the contractor in

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Comet Theatre Enterprises v. Cartwright.<sup>65</sup> In Marshall v. Von Zumwalt,<sup>66</sup> the contractor was allowed to set off the value of his services when sued by the owner for defective performance. However, there is no justification in the license statutes for these decisions.

#### COMMENT ON SECTION 7031

The writer is well aware of the need for adequate license laws. At the same time he appreciates the necessity of having adequate sanctions to impose on those failing to comply with such legislation. However, it is not believed that there is need for so drastic a penalty as that prescribed by Section 7031. It is therefore recommended that Section 7031 be revised.<sup>67</sup> The reasons for this conclusion are set out below.

(1) Any time that the cases in which exceptions to a rule are applied exceed those in which the rule is applied there is a grave question of the desirability and effectiveness of the law. As noted previously, the California courts have construed and applied Section 7031 in such a way that the policy underlying the statute has been greatly undermined. Avoidance of the forfeiture prescribed by the enactment on a broad scale clearly indicates that the courts regard the provision as too harsh. Each exception that is made denotes that the statute is opposed to justice and public policy.

The recent addition to the statute by the 1957 Legislature likewise indicates that it is unreasonable.<sup>68</sup> It can be fairly assumed that this amendment is but a beginning of a series of statutory changes that might be made from time to time when inequitable situations arise.

(2) On numerous occasions it has been stated that Section 7031 is for the protection of the public. There is a question whether the imposition of such a severe penalty is needed to protect the public. There are several other safeguards which should be adequate:

- a. By the code, contracting without a license is a criminal offense for which sanctions can be imposed.<sup>69</sup> It would appear from the published statistics that too little use is being made of the criminal section of the contractors' law.<sup>70</sup> If there were more prosecutions, unlicensed people would be deterred from violating the law.
- b. Under the possible modifications of Section 7031 discussed later, the penalty which would result would no doubt be sufficient to deter violations of the license law without the more severe forfeiture presently called for being imposed. Even if our present statute were repealed, unlicensed persons would often be denied relief by the California courts in accordance with the general rules that prevail elsewhere.<sup>70a</sup>
- c. The owner has his contract and tort remedies that he can employ in the event of nonperformance. Irrespective of whether the contractor is licensed, he is subject to contract or tort cross-claims for defective performances. However, it should be noted that there is judicial doubt as to the sufficiency of remedies under the general law for incompetency and breach of contract.<sup>71</sup>
- d. Moreover, the owner enjoys protection under the municipal building codes. Under these laws permits are necessary, plans must be approved and various inspections are required.
- (3) The penalty imposed on the unlicensed contractor by Section 7031 does not accrue to the benefit of the public, but to the owner.

Ordinarily, a penalty which is assessed against one goes to the government and thus the public is thereby benefited. Since the license statutes are for the protection of the public, and not individuals, one would expect any penalty for violation thereof to go to the State. But such is not true under Section 7031. It is the individual rather than the public that is benefited. A public statute imposes a complete forfeiture which in effect is given an individual, yet it is the public that is supposedly being protected.

(4) In effect, the statute results in unjust enrichment of the person with whom the contractor deals. Section 7031 takes property from one class of persons and gratuitously bestows it on another without hope of redress. The unlicensed contractor may do his work as well as the licensed one. In such a case the owner has no cause for complaint. But in the event that the recipient decides to avoid his obligation, the unlicensed person is left without a remedy. Therefore, the person failing to abide by the licensing requirements performs work at his own risk. He relies for performance upon the good faith of the other party. The contractor's noncompliance seems almost harmless and the real defrauder appears to be the owner who is enriching himself at the expense of the unlicensed contractor. While certainly justice requires a penalty to fit the offense, the enforcement of a license statute should not require a large forfeiture that can only benefit a repudiating owner. Therefore, the issue is whether it is sounder policy to declare a disproportionate forfeiture to aid in the enforcement of the license laws or whether it is better to permit some sort of recovery in order to avoid enrichment by a repudiating owner.

(5) If there is to be a rule of forfeiture for failure to have a license, it might be better to leave the matter to the courts to decide on

a case to case basis. It is the general rule in the United States that a party to an illegal contract cannot recover thereon if he is in pari delicto.<sup>72</sup> As has been pointed out, under this rule relief is denied by the courts on a contract made in violation of a licensing statute; thus, Section 7031 is to some extent expressive of the general law on the topic.<sup>72a</sup> While recognizing the duty to deny recovery in order to aid in the enforcement of the licensing laws, the courts are at the same time reluctant to impose a forfeiture. Consequently, the courts have developed numerous exceptions to the common law rule that there can be no recovery on an illegal contract. Under these exceptions equitable results not possible under a specific statute like Section 7031 can be reached. It is true that the California courts have made numerous exceptions to the application of the California no-action statute. However, there are instances in which recovery is allowed elsewhere which is not possible in the face of Section 7031. While courts will not generally allow recovery on an illegal contract, they nonetheless often will allow quasi-contractual recovery.<sup>73</sup> The conflict between the inequities involved in denying an unlicensed contractor of a just fee under a contract after full and satisfactory performance for failure to obtain a license, and the need for a firm license law to protect the often unwary public has frequently made fully rational results difficult to reach. Even though it is difficult to say just when relief is available under the common law rule, the general conditions governing such relief are stated as follows:

Among the factors which are or may be of importance in determining whether restitution will be granted are the following: (1) whether the complainant's conduct involved serious moral turpitude; (2) the closeness of the wrongful conduct to the transaction; (3) whether the complainant was in a superior or subservient position to the recipient; (4) how great a forfeiture would ensue from a failure to give relief; (5) whether a denial of relief would tend to discourage similar illegal transactions.<sup>74</sup>

But this relief would not be available in California. Thus, if a licensed contractor begins work on a structure and innocently permits his license to expire during performance there could be no recovery by virtue of Section 7031. Some courts would no doubt allow quasi-contractual recovery under such circumstances.

The unfairness involved in Shields v. Shoaff is in point. It will be recalled that in this case the licensee's license was automatically suspended during the performance of a contract because he innocently failed to give proper notice of the departure of his managing employee. Since Section 7031 provides for forfeiture when the contractor is not licensed throughout performance, the court denied recovery. In the absence of the California statute the court probably would have allowed recovery in quasi-contract. Yet this was not possible because of the broad mandate of Section 7031. A legislative amendment was necessary to prevent subsequent inequities along these lines.

Another example in which recovery is sometimes given is where a person performs an isolated or single act. Often it is here stated that since he is not carrying on business, relief is to be given. Yet denial of recovery for an isolated act is specifically covered in the California statute.

Should the question of forfeiture be decided by the courts, in the light of the moral turpitude of the parties, innocence of the parties, public harm involved, severity of the forfeiture that would result from a denial of relief, etc.? Or else should new legislation be enacted?

(6) It is doubtful whether Section 7031 aids substantially in the enforcement of the contractor licensing laws. One can reasonably suspect that those who are harmed most by denying relief to unlicensed persons are the

poor, innocent, well-meaning artisans, who are seeking a means of livelihood. In fact, the Contractor's State License Board has stated that "the violators are mainly newcomers to the State and those who hope to make extra money by entering into contractor's contracts as a profitable side line."<sup>80</sup>

undoubtedly, the Legislature was aware that these people are the most frequent violators.<sup>81</sup>

Would such people be encouraged to violate the license laws if the no-action statute were modified? The writer doubts if the number of violations would increase even though the State Contractor's License Board regards Section 7031 as ". . . the teeth in the contractor's license law in that it acts as a deterrent to violations of a criminal nature and therefore places this agency in a better position to regulate the industry pursuant to the statutes."<sup>81a</sup> Moreover, it should be noted that the contracting work performed by such people does not usually involve any particular skills. Therefore, this raises the propriety of our licensing scheme. This is not to say that our license statutes are unsound, however, there is an indication that the courts are not disposed towards applying the license statutes to persons who perform occasional work that does not involve any particular skill.<sup>82</sup> Assuming the validity of this point it seems that the wrongdoer in such a transaction is the owner who never has any intention to pay or who uses Section 7031 to avoid payment. As between the owner and the unlicensed contractor here, which one deserves consideration?

(7) Licenses are required for engaging in various and numerous activities. However, in only a few instances do we find specific statutes stating there can be no recovery without a license. If most of the licensing statutes can be enforced without the aid of a no-action statute, why should

not the same be true with the contractor provisions?

(8) The writer agrees that a party who is in pari delicto should not be permitted to recover for labor or services rendered under a contract that involves a serious degree of illegality or moral turpitude. Thus, a physician who practices without a license may probably endanger the health of the people. Likewise, the morals of society would be endangered if prostitution or illegal cohabitation agreements were enforced. In these instances, the extent of illegality is serious. Such is not true where one violates the contractor-license laws. The degree of illegality here is slight. While a person should not be encouraged to violate license laws, a complete forfeiture does not appear to be called for when the degree of harm or illegality is not great. At any rate, this is a matter that should be dependent upon the particular facts of a given transaction.

#### POSSIBLE SOLUTIONS

Previously, I stated that Section 7031 should be modified. The reasons for this recommendation have been set forth on the preceding pages. Assuming that a change is desirable, what are the alternatives?

(1) One alternative is to repeal Section 7031 and thereby leave the question of recovery to the courts. This would mean that relief would be granted in some cases and refused in others, depending on the various factors involved.<sup>83</sup> Thus, the courts could consider the merits of each particular case and avoid unreasonable forfeitures. Moreover, relief could be limited to the deserving against whom the public needs no protection. As already mentioned, relief, however, would often be denied in accordance with the general principles covering illegal contracts.<sup>84</sup> Since there are only 2 states<sup>85</sup> other than California that have statutes similar to Section 7031, its

repeal would place unlicensed contractors in the same position in California that they are in in other states. Moreover, the unlicensed contractor would be placed in the same position as most other unlicensed persons in California.

(2) A second alternative is the adoption of a statute providing for some measure of quasi-contractual recovery. There are two possibilities here:

- a. Section 7031 could be modified so as to allow quasi-contractual recovery for unlicensed contractors. I am not aware of any such statute having been adopted by any state. However, in those states that do not have forfeiture statutes recovery is often given on the basis of the general restitution principles. Relief in these states is no doubt more restricted than it would be under a statute specifically authorizing relief in quasi-contract.

A possible statute could be worded as follows:

No person engaged in the business or acting in the capacity of a contractor may recover more than the reasonable value of the services and goods furnished in connection with the performance of any act or contract for which a license is required by this Chapter, without alleging and proving that he was a duly licensed contractor at all times during the performance of such act or contract.

- b. A second type of quasi-contractual recovery could be provided for. Rather than giving quasi-contractual recovery for services and goods furnished, the unlicensed contractor could be awarded compensation for the goods provided, but not for the services rendered. It should be noted that the question of recovery under such a statute would vary drastically according to the type of work performed. Thus, if the contract called for the construction of a house and the contractor were to furnish the materials, he would recover anywhere from 25% to 50% of the value or cost. On the

other hand, if only services were to be performed, such as under an excavating contract, the contractor would be entitled to little, if anything. However, such a statute would partially prevent unjust enrichment and at the same time would subject the contractor to a forfeiture for his failure to comply with the license laws. To my knowledge there is no statute making this distinction in the United States. However, this is a distinction that is made by the Restatement of Restitution in certain situations. <sup>86</sup> Below is a possible statute which reflects the points made above:

No person engaged in the business or acting in the capacity of a contractor may recover more than the cost or market value, whichever is less, of goods furnished in connection with the performance of any act or contract for which a license is required by this Chapter, without alleging and proving that he was a duly licensed contractor at all times during the performance of such act or contract.

(3) Section 7031 could be modified in yet another way. A statute which provides for a penalty of a fixed percentage of the contract price could be enacted. This solution has been informally suggested by several people. Such a statute would go far towards eliminating the total windfall which the owner presently gets and at the same time the penalty involved would deter violations of the applicable license law. Again, however, I do not know of the existence of such a statute or of one similar to it. Therefore, the only authority for this scheme of legislation is the suggestions made by interested persons.

Assuming the desirability of this proposition, what percentage of forfeiture should be provided? This is a matter on which differences of opinion can reasonably exist. Ten percent would perhaps be too small and thus would be of slight, if any, deterrent value. On the other hand, the imposition of a larger

penalty would result in a great windfall to the owner. Forfeiture of 20% of the contract price, or value, seems a more satisfactory figure. Below is a proposed statute along these lines:

No person engaged in the business or acting in the capacity of a contractor may recover more than eighty (80) percent of the contract price, or value in the event of no agreement on compensation, for the performance of any act or contract for which a license is required by this Chapter, without alleging and proving that he was a duly licensed contractor at all times during the performance of such act or contract.

#### RECOMMENDATIONS

I strongly recommend the modification of Section 7031. The penalty provided thereunder is too severe as discussed previously.

A legislative solution is preferred to a judicial one. If the issue is left to the courts, it will take a long time for a scheme of recovery to be worked out. Moreover, since there are so many factors and intangibles involved in this type of problem, there would be a great degree of uncertainty. And lastly, since the license laws are of legislative origin, the rights of a party who violates them should be determined by the Legislature.

There is no authority for either of the proposed modifications mentioned above. Thus, we are not able to benefit from the experience of others. Therefore, the choice between the three remaining alternatives is a difficult one to make. I recommend a statute which would limit the unlicensed contractor's recovery to 80% of the agreed price, or of the value of the work. Care must be taken so as not to reward the contractor who fails to comply with the licensing laws. A statute giving quasi-contractual recovery for goods and services would tend to favor unduly the unlicensed party. Such generous treatment would perhaps encourage violation of the applicable laws. While justice would appear to require some recovery so as to prevent forfeiture,

the proposal that the contractor's right be limited to the market value or cost of goods or materials furnished is perhaps too harsh. As mentioned above, there would be no recovery for certain work, and only a small recovery (percentage wise) for other types under such a statute. A statute authorizing recovery of 80% of the agreed price would prevent the windfall or unjust enrichment which now occurs under Section 7031. At the same time the penalty of 20% would probably be severe enough to deter violations of the California licensing laws.

Would the suggested modification place unlicensed contractors in a better position than other unlicensed persons such as lawyers, doctors, etc.? The answer is obviously yes, however the situation would not be as drastic as it might first appear. The agreed price under a construction or repair contract is usually much greater than it is in other contracts made by unlicensed people. Hence the degree of forfeiture is greater under an agreement made by an unlicensed contractor. Moreover the degree of illegality is not nearly as great where work is performed by an unlicensed contractor as it is where services are rendered by an unlicensed lawyer or doctor.<sup>87</sup> In addition the public is protected against incompetent contractors by the local building codes which require permits, inspections, etc. There is no similar protection against incompetent and fraudulent doctors, lawyers, accountants, etc. And lastly, as previously noted, little if any special skill is required for many construction contracts. This cannot be said of the work or services rendered by other people who are required to be licensed.

FOOTNOTES

1. Cal. Stat. 1885, c. 14, p. 12.
2. N. C. Gen. Stat. Ann. §§ 87-1-8 7-13 (1949).
3. 1955 Report to the Legislature by the Senate Interim Committee on Licensing Business and Professions 163-168 (Calif.). In many states certain tradesmen who are regarded as contractors elsewhere must be licensed even though there are no contractor-licensing statutes.
4. Cal. Bus. & Prof. Code, c. 9.
5. Franklin v. Nat. C. Goldstone Agency, 33 C.2d 628, 204 P.2d 37 (1949).
6. See quotation from letter written by California Contractor's State License Board to be found in 1952 Wash. U.L.Q. 522, n. 178.
7. Calif. Stat. 1929, c. 791.
8. See note 5 supra; Howard v. State, 85 Cal. App.2d 361, 193 P.2d 11 (1948); Alvarado v. Davis, 115 Cal. App.2d 782, 6 P.2d 121 (1931).
9. Cal. Bus. & Prof. Code § 7029.
10. Cal. Bus. & Prof. Code §§ 7000-7002.
11. Cal. Bus. & Prof. Code § 7066.
12. Cal. Bus. & Prof. Code § 7137.
13. Cal. Bus. & Prof. Code § 7067.
14. Cal. Bus. & Prof. Code § 7069.
15. Cal. Bus. & Prof. Code § 7068.
16. Cal. Bus. & Prof. Code § 7072. For the results on these examinations see note 3 supra at pp. 164-68.
17. Cal. Bus. & Prof. Code § 7140.
18. Cal. Bus. & Prof. Code §§ 7090-7122.
19. Cal. Bus. & Prof. Code § 7071.5.
20. Cal. Bus. & Prof. Code § 7090.

21. Cal. Bus. & Prof. Code § 7095.
22. See *Hunt v. Douglas Lumber Co.*, 41 Ariz. 276, 171 P.2d 815 (1933). (This is considered to be the leading case on the point.)
23. *Howard v. Leiby*, 197 Ky. 324, 246 S.W. 828 (1923).
24. State ex. rel. *Sampson v. Sheridan*, 24 Wyo. 347, 170 Pac. 1 (1918).
25. *Harrigan & Reid Co. v. Burton*, 224 Mich. 564, 195 N.W. 60 (1923).
26. *Dasch v. Jackson*, 170 Md. 251, 183 Atl. 534 (1936).
27. *Old Dearborn Distributing Co. v. Seagram Distillers Corp.*, 299 U.S. 183 (1936) (Fair Trade Act); *Hall v. Geiger-Jones Co.*, 242 U.S. 539 (1917) (Sale of securities).
28. See note 8 supra.
29. Cal. Bus. & Prof. Code § 7030.
30. *Shields v. Shoaff*, 116 Cal. App.2d 306, 253 P.2d 1002 (1953).
31. Cal. Stat. 1957, c. 845, p. 2067.
32. See Clark, *Occupational Licensing in the Building Industry*, 1952 Wash. U.L.Q. 433, 531.
33. 6 Corbin, *Contracts* § 1513 (1951).
34. Ariz. Code Ann. § 67-2320 (Cum. Supp. 1951); Nev. Comp. Laws. Ann. § 1474.32A (Supp. 1949).
35. *Norwood v. Judd*, 93 Cal. App.2d 276, 200 P.2d 24 (1949).
36. A letter from the California Contractor's State Licensing Board to James D. Sumner, Jr., dated September 23, 1957.
37. See note 33 supra; Clark, *Occupational Licensing in the Building Industry*, 1952 Wash. U.L.Q. 483, 531.
38. *Gatti v. Highland Park Builders, Inc.*, 27 C.2d 867, 166 P.2d 265 (1946) (dissenting opinion).
39. *Marshall v. Von Zumwalt*, 120 Cal. App.2d 807, 262 P.2d 363 (1953).

40. 6 Corbin, Contracts § 1512 (1951).
41. Note, 43 Va. L.R. 411 (1957).
42. 6 Corbin, Contracts § 1510-14 (1951).
43. See *Albaugh v. Moss Construction Co.*, 125 Cal. App.2d 126, 269 P.2d 936 (1954); *Sheble v. Turner*, 46 Cal. App.2d 762, 117 P.2d 23 (1941).
44. *Shields v. Shoaff*, 116 Cal. App.2d 306, 253 P.2d 1002 (1953).
45. See *Cash v. Blackett*, 87 Cal. App.2d 233, 196 P.2d 585 (1948); see *Grant v. Weatherholt*, 123 Cal. App.2d 34, 41, 266 P.2d 185 (1954).
46. See *Cash v. Blackett*, 87 Cal. App.2d 233, 196 P.2d 535 (1948); *Siemens v. Meconi*, 44 Cal. App.2d 641, 112 P.2d 904 (1941).
47. *Franklin v. Nat C. Goldstone Agency*, 33 Cal.2d 626, 204 P.2d 37 (1949); *Loving & Evans v. Blick*, 33 Cal.2d 603, 204 P.2d 23 (1949).
48. *Phillips v. McIntosh*, 51 Cal. App.2d 340, 124 P.2d 835 (1942).
49. *Kirman v. Borzage*, 65 Cal. App.2d 156, 150 P.2d 3 (1944).
50. *Shields v. Shoaff*, 116 Cal. App.2d 306, 253 P.2d 1002 (1953).
51. Note 36 supra.
52. Cf. *Grant v. Weatherholt*, 123 Cal. App.2d 34, 266 P.2d 185 (1954); *Owens v. Haslett*, 98 Cal. App.2d 829, 221 P.2d 252 (1956).
- 52a. But see *Gatti v. Highland Park Builders, Inc.*, 27 Cal.2d 867, 166 P.2d 265 (1946).
53. Recovery was apparently denied in such a case under the Nevada statute; see *Bull, The Licensing of Contractors*, 17 Nev. S.B.J. 4 (1952).
54. See *Owens v. Haslett*, 98 Cal. App.2d 829, 221 P.2d 252 (1950).
- 54a. *Marshall v. Von Zumwalt*, 120 Cal. App.2d 807, 262 P.2d 363 (1953).
55. See *Dorak v. Spivak*, 107 Cal. App.2d 286, 236 P.2d 840 (1951); *Powell v. Berg*, 99 Cal. App.2d 353, 221 P.2d 743 (1950); *Malvick v. Rockwell*, 91 Cal. App.2d 463, 205 P.2d 389 (1949).

56. See Hagan v. Allen, 93 Cal. App.2d 854, 210 P.2d 65 (1949); Andrew v. Connor, 101 Cal. App.2d 621, 225 P.2d 943 (1951); Harrison v. Shamalian, 110 Cal. App.2d 500, 243 P.2d 82 (1952).
57. Cal. Bus. & Prof. Code § 7052.
58. See Oddo v. Hedde, 101 Cal. App.2d 375, 225 P.2d 929 (1950); Gatti v. Highland Park Builders, 27 Cal.2d 687, 166 P.2d 265 (1946); Citizens State Bank v. Gentry, 20 Cal. App.2d 415, 67 P.2d 364 (1937).
59. 20 Cal. App.2d 416, 67 P.2d 364 (1937).
60. 27 Cal.2d 687, 166 P.2d 265 (1946).
61. 101 Cal. App.2d 375, 225 P.2d 929 (1950).
62. See Gatti v. Highland Park Builders, 27 Cal.2d 687, 691, 166 P.2d 265, 267 (1946) (dissenting opinion).
63. Matchett v. Gould, 131 Cal. App.2d 821, 281 P.2d 524 (1955); Wilson v. Stearns, 123 Cal. App.2d 472, 267 P.2d 59 (1954). The Matchett case was recently disapproved in Lewis & Queen v. N. M. Ball Sons, 48 Cal.2d 141, 308 P.2d 713 (1957) and Harrison v. Butte Steel Bldg., Inc., 150 Cal. App.2d 296, 310 P.2d 126 (1957).
64. Norwood v. Judd, 93 Cal. App.2d 276, 209 P.2d 24 (1949).
65. 195 F.2d 80 (9th Cir. 1952).
66. 120 Cal. App.2d 807, 262 P.2d 363 (1953).
67. There have also been pleas for the repeal of the Nevada no-action statute. Bull, The Licensing of Contractors, 17 Nev. S.B.J. 4 (1952).
68. See notes 30 and 31 supra.
69. Cal. Bus. & Prof. Code § 7030.
70. According to the statistics published by the Contractor's State License Board there were only 416 convictions of non-licensees for the year 1956-57. The balance of a total of 2878 complaints was disposed of in the following manner: Insufficient evidence to

prosecute - 1685; citation refused - no court action - 551; not guilty by court - 31; unable to serve warrant - 195.

70a. In general see *Lewis & Queen v. N. M. Ball Sons*, 48 Cal.2d 141, 308 P.2d 713 (1957) and *Harrison v. Butte Steel Bldgs., Inc.*, 150 Cal. App.2d 296, 310 P.2d 126 (1957).

71. See *Howard v. State*, 85 Cal. App.2d 361, 366, 193 P.2d 11 (1948).

72. 6 Corbin, *Contracts* § 1373 (1951).

72a. See note 70a supra.

73. For a discussion of the issue and complete citation of cases, see 6 Corbin, *Contracts* §§ 1535-40 (1951).

74. *Restatement, Restitution* § 140, comment b (1936).

75. See note 73 supra.

76. 116 Cal. App.2d 306, 253 P.2d 1002 (1953).

77. Cal. Bus. & Prof. Code § 7068.

78. See *Albaugh v. Moss Construction Co.*, 125 Cal. App.2d 126, 269 P.2d 936 (1954); *Sheble v. Turner*, 46 Cal. App.2d 762, 117 P.2d 23 (1941).

79. The cases are collected in Notes: 30 A.L.R. 834, 858; 42 A.L.R. 1226, 1230; 118 A.L.R. 646, 657.

80. See note 36 supra.

81. See note 3 supra at pp. 62-67.

81a. See note 36 supra.

82. See note 55 supra.

82a. Cal. Bus. & Prof. Code § 8554 (pest control); Cal. Bus. & Prof. Code § 9678 (cemetery brokers and salesmen); Cal. Bus. & Prof. Code § 10136 (real estate brokers and salesmen); Cal. Bus. & Prof. Code § 10257 (business opportunity brokers and salesmen) and Cal. Bus. & Prof. Code § 10508 (mineral, oil and gas brokers and salesmen).

83. See note 74 supra.

84. See note 37 supra.

85. See note 34 supra.

86. Restatement, Restitution § 41 (1936).

87. See Harrison v. Butte Steel Bldgs., Inc., 150 Cal. App.2d 296, 301,  
310 P.2d 126 (1957).